IN THE

Supreme Court of the United States

OCTOBER TERM, 1936

No. 602

GALEN H. WELCH, *Former Collector of Internal Revenue for the Sixth Collection District of California, Petitioner,*

v.

OBISPO OIL COMPANY, *a Corporation*

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF OF AMICUS CURIAE

PERCY W. PHILLIPS,
Southern Building,
Washington, D. C.

Of Counsel:
IVINS, PHILLIPS, GRAVES & BARKER,
Washington, D. C.

INDEX

PAGE

PETITION FOR LEAVE TO FILE BRIEF AMICUS CURIAE 1

BRIEF OF AMICUS CURIAE 2

Introduction 2

Brief of Argument 3

Argument 3

I. Special assessment has often been thrust upon a taxpayer without his request, without any agreement on his part as to the net income, and over his protest 3

II. The statute does not permit the special assessment section to be used to increase the tax beyond that imposed at the statutory rates 9

III. The position of the Collector is contrary to precedent, is unjust and is unnecessary 10

Conclusion 12

TABLE OF CASES

Austin Co. v. *Commissioner*, 35 Fed. (2d) 910 9

Botany Worsted Mills v. *United States*, 278 U. S. 282 4

Brownsville Bridge Co. v. *Commissioner*, 1 B. T. A. 320 10

Heiner v. *Diamond Alkali Co.*, 288 U. S. 502 ..... 2, 11, 12

McGrath Co. v. *Commissioner*, 10 B. T. A. 177 6

Oak Worsted Mills v. *United States*, 38 Fed. (2d) 699 9

Sumpter Valley Railway Co. v. *Commissioner*, 10 B. T. A. 1325 ..... 7, 10

United States v. *Supplee-Biddle Hardware Co.*, 265 U. S. 189 ..... 2, 8, 9, 11

United Profit Sharing Corp v. *United States*, 66 Ct. Cl. 171 ..... 7, 10

Williamsport Wire Rope Co. v. *United States*, 277 U. S. 551 ..... 2, 11, 12

PAGE

A. R. R. 19, 2 Cumulative Bulletin 299 5
A. R. R. 70, 2 Cumulative Bulletin 287 4
A. R. R. 332, 3 Cumulative Bulletin 362 5
A. R. R. 459, 4 Cumulative Bulletin 399 5
A. R. R. 538, 5 Cumulative Bulletin 301 5
Sol. Op., III-1 Cumulative Bulletin 418 10

Revenue Act of 1917, Section 210 4
Revenue Act of 1918, Section 302 9

IN THE

Supreme Court of the United States

OCTOBER TERM, 1936

No. 602

GALEN H. WELCH, *Former Collector of Internal Revenue for the Sixth Collection District of California, Petitioner,*

v.

OBISPO OIL COMPANY, *a Corporation*

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

PETITION FOR LEAVE TO FILE BRIEF AMICUS CURIAE

The undersigned respectfully petition this Court for leave to file the subjoined brief as a friend of the Court.

PERCY W. PHILLIPS,
Southern Building,
Washington, D. C.

Of Counsel:
IVINS, PHILLIPS, GRAVES & BARKER,
Washington, D. C.

BRIEF OF AMICUS CURIAE

INTRODUCTION

It is an undisputed principle of the law that the courts have jurisdiction in the proper case to recompute the tax liability of a taxpayer. In *Williamsport Wire Rope Co.* v. *United States*, 277 U. S. 551, and *Heiner* v. *Diamond Alkali Co.*, 288 U. S. 502, this Court held that the courts might not review the exercise of an administrative discretion by the Commissioner of Internal Revenue. The soundness of those decisions is not questioned.

It will be the purpose of this brief, however, to point out that those decisions should not be extended to deprive the courts of jurisdiction to compute the tax under statutory provisions which involve no exercise of administrative discretion.

In *Heiner* v. *Diamond Alkali Co.*, *supra*, this Court said:

> "The respondent's tax could only be computed in accordance with Section 301 or under Section 328. The former prescribes the elements to be considered and *error in the computation remains subject to judicial correction.*"

We conceive the instant case to be an attack upon that statement and an attempt to reverse the decision of this Court in *United States* v. *Supplee-Biddle Hardware Co.*, 265 U. S. 189. In that case the tax had been computed by the Commissioner under the special assessment provision. This Court, however, found no difficulty in determining the tax under the statutory provisions and affirming the judgment of the lower court for the recovery of the difference between the tax computed by the Commissioner under the special assessment rates and the tax at the statutory rates upon the revised income determined by the court.

It would seem a matter of course that while the courts may not grant special assessment or recompute the tax payable under the special assessment provision, they may determine the tax liability under those provisions of the statute which involve no discretion and, if the tax has been overpaid, give judgment for the overpayment.

BRIEF OF ARGUMENT

Special assessment has often been thrust upon a taxpayer without his request, without any agreement on his part as to the net income, and over his protest. The statute does not permit the special assessment section to be used to increase the tax beyond that imposed at the statutory rates. The position of the Collector is contrary to precedent, is unjust and is unnecessary. The Commissioner of Internal Revenue may not deprive the courts of jurisdiction to compute tax under the plain provisions of the statute which involve no exercise of administrative discretion by insisting upon determining the tax under the special assessment provisions. To so hold would place the taxpayer in the uncontrolled discretion of the Commissioner. It would permit a relief provision to be used to impose taxes in excess of those imposed by Congress and leave the taxpayer with no recourse to the courts.

ARGUMENT

I. Special assessment has often been thrust upon a taxpayer without his request, without any agreement on his part as to the net income, and over his protest.

It seems to be taken for granted in some of the decisions upon which the Collector relies in his brief that special assessment is granted only when the taxpayer and the Commissioner are agreed upon the factors to be used. Assum-

ing this as a fact, the decisions proceed by way of semi-estoppel[1] to reach the conclusion, not that the taxpayer may not recover in that particular case, but to hold that the granting of special assessment deprives the courts of any jurisdiction to entertain a suit to determine the tax under statutory rates involving the exercise of no administrative discretion. The history of the administration of this section contradicts any thought that the taxpayer was required to agree to the correctness of the determination of its income and make a request for special assessment before the tax was computed under the special assessment sections. Perhaps this should have been the practice, but it was not.

In a ruling made by the Committee on Appeals and Review in the office of the Commissioner of Internal Revenue in 1920,[2] it appeared that the taxpayer corporation claimed the right to have its invested capital determined by including therein the value of a certain patent and, presumably, its net income computed by allowing a deduction for the amortization or exhaustion of the patent value. The Committee stated that the value of the patent "cannot be satisfactorily determined". The opinion concludes:

> "The Committee is therefore of the opinion that the action of the Income Tax Unit in assessing the tax under the provisions of Section 210[3] was proper and works no injustice upon the taxpayer. For the same reason that Section 210 was applied under the 1917 Act, it is recommended that the company be assessed for 1918 and subsequent years under the provisions of Sections 327 and 328 of the Revenue Act of 1918."

---

[1] But see *Botany Worsted Mills* v. *United States*, 278 U. S. 282, which outlines the only basis on which a binding agreement as to tax liability may be reached.

[2] A. R. R. 70, 2 Cumulative Bulletin 287.

[3] Section 210 of the Revenue Act of 1917 was the special assessment provision of that Act.

In A. R. R. 19, 2 Cumulative Bulletin 299 (1920), the Committee found difficulty in arriving at the facts, whereupon the Committee ruled:

> "The Committee is of the opinion that the facts, so far as they are known or asserted by the taxpayer, construed in the light of the regulations above quoted, clearly exclude the taxpayer from whatever benefit might be derived from the application of Section 209 of the Revenue Act of 1917, and therefore the Committee recommends that the appeal of the taxpayer for consideration under that section be denied and that the action of the Income Tax Unit in assessing tax under Section 210 of the above Act be approved and confirmed."

In A. R. R. 332, 3 Cumulative Bulletin 362 (1920), the following appears:

> "The taxpayer submits that the assessment under Section 210 imposes too high a tax, and that in lieu thereof the tax should be based on certain other methods of determining invested capital, which it does not seem necessary to now refer to in detail. • • • The Committee recommends that action of the Income Tax Unit in assessing the tax under Section 210 of the Act be sustained."

In A. R. R. 459, 4 Cumulative Bulletin 399, the following appears:

> "The Committee has had under consideration the appeal of the M Company, a corporation, from the action of the Income Tax Unit in assessing taxes for the year 1917 under Section 210 instead of under Section 207 of the Revenue Act of 1917. • • • The Committee accordingly recommends that the action of the Income Tax Unit, in disposing of this case under Section 210 of the Revenue Act of 1917, be sustained."

In A. R. R. 538, 5 Cumulative Bulletin 301, the following appears:

"The Committee has had under consideration the appeal of the M Company, formerly the N Company, from the action of the Income Tax Unit in computing the amount of war-profits credit to be allowed the corporation for the year 1918 under the provisions of Section 311(a) of the Revenue Act of 1918 and including in the closing inventory for that year the amount of fruit on hand in warehouses ready for sale. * * * In view of the foregoing, the Committee recommends that the M Company, formerly the N Company, be granted the benefit of assessment of excess-profits and war-profits taxes for the year 1918 under the provisions of Section 327 and 328 of the Revenue Act of 1918; that in the preparation of a comparative data sheet particular care be used to select only such comparatives as are fair both to the Government and to the taxpayer; and that the Unit be sustained in restoring to the closing inventory for that year the fruit on hand in warehouses and in transit to market, but not marketed and sold as of December 31, 1918."

While the earlier citations were under the Revenue Act of 1917, this decision of the Committee on Appeals and Review makes it clear that under the 1918 Act the Commissioner continued to compute taxes under the special assessment sections without first agreeing with the taxpayer upon the amount of its net income subject to the tax and, indeed, without any request for special assessment from the taxpayer.

Counsel has made an examination of Volume 10 of the reports of the United States Board of Tax Appeals. This volume covers the decisions rendered in two months of the year 1928 and was selected because it was in this period that the claim of the Obispo Oil Company was rejected by the Commissioner.

In *William McGrath Co.* v. *Commissioner*, 10 B. T. A. 177, it appeared that the Commissioner had computed the profits

tax for 1918 under the special assessment provision. The taxpayer there was contending that it had a right to have its tax computed at the statutory rates, while the Commissioner was contending that the invested capital could not be ascertained and that the Commissioner properly computed the tax under the special assessment provisions. The Board of Tax Appeals, however, found that the invested capital could be ascertained and directed the computation of the tax at the statutory rates.

Sumpter Valley Railway Co. v. *Commissioner*, 10 B. T. A. 1325, was a similar case. There the Board said:

> "Sections 327 and 328 have been held to be relief sections, and they cannot be used to impose upon a taxpayer a greater tax than he would have to pay under Section 326."

These are merely two examples from one volume of the Board of Tax Appeals Reports cited to establish the fact that special assessment was not something granted only at the request of the taxpayer, but was imposed by the Commissioner without request and over the protest of the taxpayer. Without doubt, an examination of the 34 volumes of those Reports would disclose many other such cases.

We find the same situation in some of the reported decisions of the courts. In *United Profit-Sharing Corp.* v. *United States*, 66 Ct. Cl. 171, it appears from the opinion of the court that in the years 1914, 1915 and 1916 the plaintiff made large expenditures which it charged to expense account. In filing returns for the years 1919 and 1920, it claimed that such a treatment was in error; that such expenditures were in fact capital expenditures and should be amortized over a period of years, including the years 1919 and 1920; that the income for those years should be reduced by an aliquot portion as amortization or exhaus-

tion in those years, and that the invested capital should include the unamortized amount of such expenditures. The Commissioner had refused to permit the invested capital or the income to be computed on that basis and, on the contrary, had determined that the tax should be computed under the special assessment provisions. The Court of Claims held that the contentions of the plaintiff were correct; that its income and invested capital should be adjusted accordingly and its tax computed under the statutory provisions.

In *United States* v. *Supplee-Biddle Hardware Co., supra,* a somewhat similar situation was presented to this Court. The Commissioner had held that the proceeds of certain life insurance policies should be included in computing the income of the taxpayer. Under this ruling the taxpayer was forced to pay a tax of $84,737.95. The Commissioner reduced this amount by $29,584.06 by computing tax under the special assessment provisions. There remained, however, the sum of $55,153.89 which was paid under protest. This Court proceeded to determine the issue upon its merits. It held that the proceeds of life insurance paid to a corporation were not taxable income under the provisions of the Revenue Act; that the Commissioner had erroneously included such amount, and that the taxpayer was entitled to recover.

We believe these cases conclusively establish that the Commissioner of Internal Revenue frequently applied the special assessment provisions of the Revenue Act without any agreement on the part of the taxpayer as to the amount of its income or invested capital, and at times when the amount of income and invested capital was in dispute. They also make it clear that the courts in the past have not hesitated to determine the tax at the rates prescribed by Con-

gress and grant refunds where excessive tax was assessed under the special assessment provisions.

There is another line of decisions which indicates that the exercise of the Commissioner's discretion under the special assessment sections lacks any finality.

In *Oak Worsted Mills* v. *United States*, 38 Fed. (2d) 699, it appeared that the Commissioner had determined the profits tax under the special assessment provisions. Subsequently he reopened his determination and computed and collected a greater tax. The court held that the Commissioner might reopen his determination at any time within the statute of limitations without regard to the existence of fraud.

In *Austin Co.* v. *Commissioner of Internal Revenue*, 35 Fed. (2d) 910, the Circuit Court for the Sixth Circuit had before it a similar case and reached the same decision.

II. The statute does not permit the special assessment section to be used to increase the tax beyond that imposed at the statutory rates.

Congress provided the rates at which taxes should be computed. It then imposed certain limitations on those taxes[1] and also provided that in certain cases the Commissioner should compute taxes by comparison with representative corporations. The history of these sections discloses that they were intended to extend relief to the taxpayers, and clearly shows that they were not intended for the purpose of increasing the taxes beyond those imposed by Congress at the statutory rates.

Perhaps it would be sufficient to cite the decision of this Court in *United States* v. *Supplee-Biddle Hardware Company, supra*, in which this Court permitted the taxpayer to recover the difference between the tax assessed and collected under the special assessment provisions and the tax properly computed at the statutory rates, or the decision

[1] Section 302, Revenue Act of 1918.

of the Court of Claims in *United Profit-Sharing Corporation* v. *United States, supra.* Counsel, however, would refer this Court to certain other sources. In the opinion of the Solicitor of Internal Revenue, No. 158, published in III-1 Cumulative Bulletin 418 (1924), the legislative history is considered at very considerable length, and the opinion states:

> "On the contrary, they were constantly referred to as 'relief measures' and are so characterized in Law Opinion 1109."

The Committee on Appeals and Review of the Treasury Department in 3 Cumulative Bulletin 360 (1920) said:

> "This office, therefore, concludes that special assessment is not required by either the Revenue Act of 1917 or 1918 when the tax computed upon the basis of the known invested capital is less than that computed under special assessment."

To the same effect are the decisions of the Board of Tax Appeals in *Brownsville Bridge Co.* v. *Commissioner*, 1 B. T. A. 320, and *Sumpter Valley Railway Co.* v. *Commissioner, supra.*

When the legislative history so clearly discloses that the special assessment provisions were intended for the relief of taxpayers, it is submitted that neither the Commissioner nor the courts should use them as a means to deprive the courts of jurisdiction to compute the amount of tax which is due under the rates imposed by the law. An instrument of relief should not be used as an instrument of oppression.

III. The position of the Collector is contrary to precedent, is unjust and is unnecessary.

It has been shown that special assessment was often thrust upon the taxpayer when the Commissioner was un-

able to agree with the contentions of the taxpayer with respect to invested capital, or with respect to taxable income. The decisions of the courts demonstrate that the Commissioner is frequently wrong in his determinations. Is there anything in the law which prohibits the courts from taking jurisdiction to correct those errors? In the *Supplee-Biddle Hardware Company* case we have a practical application of the question. The Commissioner insisted that certain amounts should be included in taxable income. The taxpayer resisted that determination. The Commissioner then computed the tax under special assessment. The contention of the appellant is, in effect, that under such circumstances no court could inquire into the correctness of the determination of the amount of the income, despite the fact that this Court found that the action of the Commissioner resulted in an overpayment of the tax by $55,153.86. The Court will recognize that if the contention of the appellant is sound, the taxpayer is entirely at the mercy of the Commissioner. All that the Commissioner need do is to determine that the tax should be computed under special assessment; thereafter the taxpayer will have no recourse to the courts. If the contention of the appellant is correct, this Court had no authority in the *Supplee-Biddle Hardware Company* case to inquire into the determination of the income or of the tax and the overpayment made by the taxpayer could not have been refunded to it.

It seems to us ridiculous to contend that the decisions of this Court in *Williamsport Wire Rope Company* and *Diamond Alkali Company, supra,* go to any such extremes. Those cases decide that the courts will not grant special assessment where the Commissioner denies it, and that the courts will not compute or recompute the tax due under the special assessment sections. Certainly they do not stand for the proposition that the courts may not determine the

tax which is due under the rates prescribed by Congress in the law.

In the instant case the law prescribes an income tax at the rate of ten per cent upon the statutory income. The elements which go into the computation of statutory income are carefully laid down in the statute, and as the court stated in *Heiner* v. *Diamond Alkali Company, supra,* are "subject to judicial correction."

CONCLUSION

It is respectfully submitted that the special assessment provisions of the Revenue Act were intended for the purpose of relieving the taxpayers and not as an excuse or trap for denying them the right to a proper computation of taxes, either in the Bureau of Internal Revenue or in the courts. It is further submitted that until very recently no contention had been made in the Bureau of Internal Revenue or in the courts that the granting of special assessment deprived the courts of jurisdiction to determine the proper tax at the statutory rates. It is further submitted that there is nothing in the decisions of this Court in *Williamsport Wire Rope Company, Heiner* v. *Diamond Alkali Company,* or in any other case, which justifies any conclusion that the courts may be ousted of their jurisdiction to determine the tax liability of a taxpayer at the rates prescribed by statute merely because the Commissioner of Internal Revenue sees fit to incorrectly determine the income of the taxpayer or the invested capital of the taxpayer and, on such erroneous determination, to compute a tax under the special assessment provisions of the law. It is part of the system for the collection of our taxes that the courts should review the determination of the tax liability and, while the courts will not review the determination of the tax under the special assessment provisions,

those provisions should not be used as a means of ousting the courts from jurisdiction to compute a tax under the plain provisions of the Revenue Act which are susceptible of judicial application.

Respectfully submitted,

PERCY W. PHILLIPS,
Southern Building,
Washington, D. C.

Of Counsel:
IVINS, PHILLIPS, GRAVES & BARKER,
Washington, D. C.